

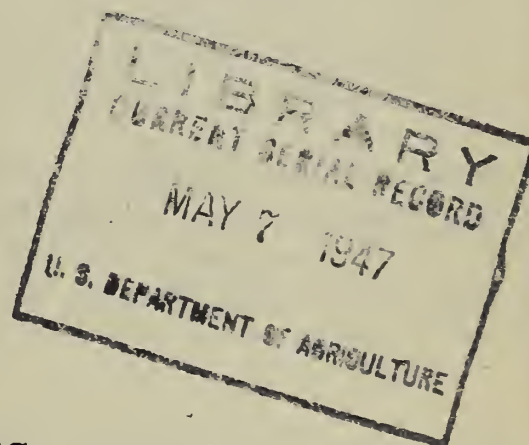
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FARM CREDIT ADMINISTRATION
UNITED STATES DEPARTMENT OF AGRICULTURE
WASHINGTON, D. C.

x PREPARING FEDERAL ANNUAL RETURNS
FOR TAX-EXEMPT FARMERS' COOPERATIVES x



By
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UNITED STATES DEPARTMENT OF AGRICULTURE
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This report covers the preparation of Federal annual returns required of tax-exempt farmers' cooperatives on Treasury Department form 990, as revised in January 1947.

It supersedes the publication, issued July 12, 1944, entitled "Suggestions Relating to the Filing of Annual Information Returns by Farmers' Marketing and Purchasing Associations," by Kelsey B. Gardner of the Cooperative Research and Service Division, Farm Credit Administration. Mr. Gardner's publication dealt with the preparation of the old form 990 as revised in May 1944.

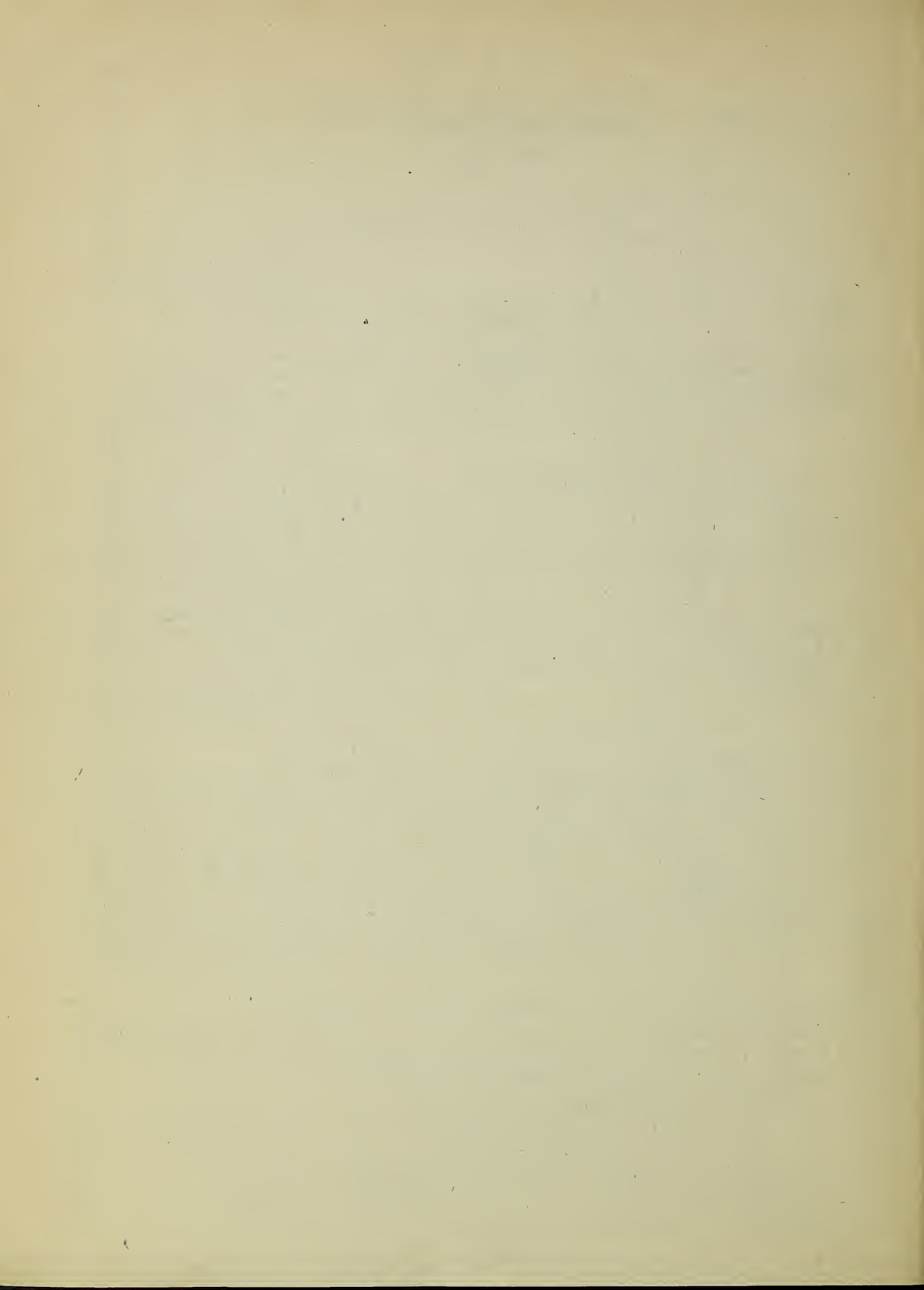
Form 990, as revised in January 1947, must be used for returns covering fiscal years beginning *after* December 31, 1945. It must be filed on or before the 15th day of the 5th month following the close of the reporting organization's fiscal year.

The Cooperative Research and Service Division conducts research studies and service activities relating to problems of management, organization, policies, merchandising, sales, costs, competition, and membership arising in connection with the cooperative marketing of agricultural products and the cooperative purchase of farm supplies and services; publishes the results of such studies; confers and advises with officials of farmers' cooperative associations; and cooperates with educational agencies, cooperative associations, and others in the dissemination of information relating to cooperative principles and practices.

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DIRECTOR OF INFORMATION AND EXTENSION
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U. S. DEPARTMENT OF AGRICULTURE
WASHINGTON 25, D. C.

TABLE OF CONTENTS

	Page
General remarks.....	1
Significance of amplified return.....	2
Who is to file the revised form 990?.....	3
Proof of exemption.....	3
Return period, filing date, etc.....	3
Failure to file a return.....	4
Statute of limitations.....	4
Amended returns.....	4
Change of fiscal year.....	4
Review of revised form 990 and of the instructions printed thereon.	5
Preparation of upper portion of page 1, revised form 990.....	5
Comments on each item of upper portion of page 1.....	6
Preparation of lower portion of page 1, revised form 990.....	7
Comments on items:	
1, 2, 3, and 4 of page 1	7
5 and 6 of page 1.....	8
7, 8, and 9 of page 1.....	9
10, 11, 12, and 13 of page 1.....	11
14(a) of page 1.....	11
14(b) of page 1.....	12
14(c) of page 1.....	13
14(d) of page 1.....	14
14(e) of page 1.....	15
14(f) of page 1.....	16
Preparation of operating statement (on page 2 of revised form 990).	17
Accrual basis.....	17
Cash basis.....	18
Comments on items:	
1 and 2 of page 2.....	20
3, 4, 5, and 6 of page 2.....	20
7 of page 2.....	21
Typical entries for gross receipts from business activities (Table A).....	22
8 and 9 of page 2.....	23
10 and 11 of page 2.....	24
12 of page 2.....	24
13 through 19 of page 2.....	25
20 through 26 of page 2.....	26
27, 28, and 29 of page 2.....	26
30 and 31 of page 2.....	27
32 of page 2.....	29
33 and 34 of page 2.....	30
Preparation of schedule A, balance sheets (on page 3 of revised form 990).....	30
Asset accounts.....	30
Liability accounts, etc.....	31
Comments on items:	
11, 12, and 13 of page 3.....	31
14 and 15 of page 3.....	31
16, 17, and 18 of page 3.....	32
Preparation of schedule B, gains and losses from sales of assets, etc. (on page 3 of revised form 990).....	32
Execution of declarations (on page 4 of revised form 990).....	33



PREPARING FEDERAL ANNUAL RETURNS FOR TAX-EXEMPT FARMERS' COOPERATIVES

By

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GENERAL REMARKS

For many years the regulations¹ of the Bureau of Internal Revenue have required certain organizations exempt from Federal income taxation to make an annual information return on Treasury Department form 990, entitled "Annual Return of Organization Exempt From Income Tax Under Section 101 of the Internal Revenue Code, or Under Corresponding Provisions of Prior Revenue Acts." Such returns were used mainly to determine whether or not exemption eligibility was being maintained by the reporting organizations.

Through the Revenue Act of 1943, passed in February 1944, Congress extended the filing requirements to a number of other groups of exempt organizations.² Included in those groups were organizations exempt under section 101(12) of the Internal Revenue Code, namely, farmers' cooperatives engaged in marketing, purchasing, and related operations (including bargaining and servicing or processing connected with agricultural production or marketing, or with the purchasing of farm supplies and equipment) and organizations exempt under section 101(13) of the Code, namely, crop financing cooperatives operated in conjunction with tax-exempt farmers' marketing or purchasing associations.

For convenience, the organizations covered by sections 101(12) and 101(13) will be referred to herein as tax-exempt farmers' cooperatives. It is to these cooperatives that the following comments primarily are directed. Some of the comments, however, also will apply to mutual ditch or irrigation companies which are tax-exempt under section 101(10) of the Code.

Administration of the Federal income tax and tax-exemption provisions is vested solely in the Treasury Department through its Bureau of

¹The regulations, as amended June 26, 1944, by T. D. 5381, relating to the filing of annual returns by certain tax-exempt organizations, including farmers' cooperatives, appear in the supplement to Regulations 111, Income Tax, Internal Revenue Code, pp. 181-185.

²See section 54(f) of the Internal Revenue Code, as amended by section 117(a) of the Revenue Act of 1943.

NOTE: Acknowledgement is made to L. S. Hulbert, Chief, and Russell D. Burchard, Attorney, of the Cooperative Bank and Cooperative Research Division, Office of the Solicitor, United States Department of Agriculture, and to Kelsey B. Gardner, Principal Agricultural Economist of the Cooperative Research and Service Division, Farm Credit Administration, for valuable assistance in the preparation of this report.

Internal Revenue. The Cooperative Research and Service Division of the Farm Credit Administration, through statutory authority for cooperative research, service, and educational activities presents this report as an informational service to the management and advisors of farmers' cooperatives and to others interested in their welfare. It is hoped that this material will be of assistance to those parties in complying with the requirements for filing of the annual return and in preparing it so as to reflect correctly the cooperative character of the organizations they represent.

The return blank (revised form 990) is designed to be used by a variety of tax-exempt organizations, in addition to farmers' cooperatives. The inherent characteristics of cooperative organization and operation, contrasted with those of other types of businesses, form the basis for the main part of the special explanations and suggestions contained in this report.

Although the contents of this publication have been discussed informally with officials of the Bureau of Internal Revenue, the report is not to be considered as binding upon either the Bureau, the Farm Credit Administration, or the United States Government itself. In fact, it is suggested that whenever necessary, cooperatives should consult their local attorneys, public accountants, collectors of internal revenue, or other competent persons for advice on specific matters relating to tax-exemption and the preparation of related forms or returns.

Tax-exempt farmers' cooperatives first began filing these annual returns on form 990 (as revised May 1944) for fiscal years beginning after December 31, 1942. The form was slightly revised in January 1946. It was again revised in January 1947, and then expanded from two to four pages with numerous important changes and additions. It is with form 990, as revised in January 1947, that this report deals.

SIGNIFICANCE OF AMPLIFIED RETURN

The expanded and revised return now calls for additional information and statistics, and inquires into many of the detailed operating practices of tax-exempt farmers' cooperatives.

It is important that farmers' cooperatives take *meticulous care* each year in the *accurate and complete* preparation of the revised form 990. It cannot be emphasized too strongly that *every* item on the form which is found applicable to your organization must be carefully and completely answered. Furthermore, the preparation of this important return should be entrusted only to one who is capable of careful attention to details and who is thoroughly familiar with all phases of the reporting organization's operations.

It is now more than ever desirable, if not necessary, that farmers' organizations, in submitting or issuing any financial data, should use the newer and advanced terminology which portrays cooperative organizations in their true mutual, cooperative character.

Shortly after the passage of the Revenue Act of 1943, the Committee on Ways and Means, House of Representatives, made the statement regarding both agricultural and nonagricultural exempt organizations " * * * that many of these exempt corporations and organizations are directly competing with companies required to pay income taxes, and that this practice is becoming more widespread and affording a loophole for tax evasion and avoidance." The Committee further stated that it intended " * * * to make a thorough study of the information contained in such returns with the view to closing this existing loophole and requiring the payment of tax, and the protection of legitimate companies against this unfair competitive situation."

WHO IS TO FILE THE REVISED FORM 990?

As to farmers' cooperatives, an annual return on the revised form 990 is required *only* of those organizations (1) which have been ruled to be exempt and, therefore, have received a "letter of exemption" from the Commissioner of Internal Revenue, or (2) which have made proper application for affirmation of their exempt status on Treasury Department form 1028 but have not yet received the Commissioner's determination of their status.³

It should be understood that revised form 990 is to be filed whether the cooperative is a corporation, or merely an unincorporated association.

PROOF OF EXEMPTION

A farmers' cooperative which claims to be exempt from Federal income taxes but which does *not* hold a letter of exemption, is required to prove its exemption by application on form 1028, at or prior to the time when information returns on form 990 are due. If the cooperative fails to file proof of exemption, or upon filing is held ineligible for exemption, then it must file an income tax return annually, or until such time as it may qualify for exemption. Such tax returns are made on Treasury Department form 1120. Blanks therefor may be obtained from the local collector of internal revenue with whom the completed return should be filed.

RETURN PERIOD, FILING DATE, ETC.

The Bureau of Internal Revenue has ruled that form 990 (as revised January 1947) must be filed for the fiscal years of reporting organizations beginning *after* December 31, 1945. This means that organizations which have already used the old form 990 in reporting for periods beginning after December 31, 1945, will be expected to *re-file* on the revised form 990.

³For information on the filing of form 1028, and on the specific requirements for tax exemption, see "Application of the Federal Income Tax Statutes to Farmers' Cooperatives," Farm Credit Administration, Bul. No. 53, by George J. Waas and Daniel G. White, or "Legal Phases of Cooperative Associations," Farm Credit Administration, Bul. No. 50, by L. S. Hulbert. If a condensed reference is desired, see "Farmers' Cooperatives and the Federal Income Tax Statutes," Farm Credit Administration, Misc. Report 75, by Kelsey B. Gardner. Copies of these publications may be obtained upon request of the Director of Information and Extension, Farm Credit Administration, United States Department of Agriculture, Washington 25, D. C.

Actual filing must be made on or before the 15th day of the 5th month following the close of the cooperative's annual accounting period. Thus, the earliest filing deadline for the *revised* form 990 is May 15, 1947, which is applicable to organizations whose fiscal year ended December 31, 1946. The return must be filed with the collector of internal revenue for the district in which is located the principal place of business or principal office of the reporting organization. Blank forms for the return may be obtained from the local collector.

FAILURE TO FILE A RETURN

Tax-exempt organizations which fail to file form 990 annually, as required, are not subject to a monetary penalty for such failure. Any willful failure of that kind, however, would be followed without any doubt by the Bureau's revocation of the organization's tax-exempt status. The organization, thereupon, would be required to file an income tax return on form 1120.

STATUTE OF LIMITATIONS

In the case of taxable businesses, the Federal limitations statute bars the Government from making an assessment of taxes after expiration of 3 years from the date of filing an income tax return, except where the latter is fraudulently made.

While an official ruling has not yet been published by the Bureau of Internal Revenue, it is understood informally that the 3-year period of limitations is started in the case of tax-exempt organizations upon their filing of form 990 provided, of course, that the return is *full and complete*.

AMENDED RETURNS

In cases where a farmers' cooperative, after filing an annual return on form 990 discovers an error therein or determines that the form was not filled in completely, an amendment or revision of the return may be filed with the local collector of internal revenue. If the changes are minor, this may be done in the form of a letter; otherwise, another blank printed form 990 should be used, showing clearly thereon the words, "Amended Return."

There is no time limit for the filing of an amended return. It should be kept in mind that each return represents the situation existing *only* for the year concerned and, therefore, does not act as an automatic corrective of prior returns. Amended returns, however, should *not* be filed to cover insignificant items.

CHANGE OF FISCAL YEAR

If, after application to the Bureau of Internal Revenue (on Treasury Department form 1128), a cooperative association secures permission to

change its fiscal year, it must file form 990 (as revised January 1947) for the short period involved. For example, an association properly filed a form 990 for its fiscal year ended December 31, 1946, and, thereafter, its fiscal year was changed to end on June 30. In such a case, a return on form 990 must be filed for the short period from January 1 to June 30, 1947. Henceforth, of course, the organization will simply file a return for each fiscal year ending June 30.

In no case should a form 990 be filed for a period greater than 12 months.

REVIEW OF REVISED FORM 990 AND OF THE INSTRUCTIONS PRINTED THEREON

Before attempting to prepare the annual return on revised form 990, it is suggested that the four pages of the form first be given a careful scrutiny. As pointed out previously, the form was designed to be used by a considerable variety of organizations, in addition to farmers' cooperatives. Because of this, the wording and set-up had to be generalized in some instances.

At least one exact copy of the return should be retained by your organization for future reference. It will be found of use in making the succeeding year's return. Having before you a copy of the association's application (on Treasury Department form 1028) for a letter of exemption may be helpful also in preparing some portions of the annual return (revised form 990).

The next logical step is to review the instructions appearing on page 4 of the annual return so as to secure a thorough understanding of them. Only a few highlights among these instructions will be discussed in this report.

Instruction 2, page 4 of the revised form 990, states that the form shall be prepared in accordance with the method of accounting regularly employed in keeping the books of your organization. Among other things, this means that the form may be filled out on either the cash or the accrual basis of accounting. (Question 11, on page 1 of revised form 990, indicates this option.)

Instruction 4, on page 4 of the revised form 990, refers to the filing of a group return by certain affiliated organizations. The Bureau of Internal Revenue has ruled that the group return method shall *not* be used by farmers' cooperatives exempt under either section 101(12) or 101(13) of the Code.

PREPARATION OF UPPER PORTION OF PAGE 1, REVISED FORM 990

Following is a facsimile of part of the upper portion of page 1, revised form 990.

For Calendar Year _____
or Fiscal Year Begun _____, and Ended _____

PRINT PLAINLY NAME AND ADDRESS OF THE ORGANIZATION		
<div style="border-top: 1px dashed black; height: 1.2em; margin-bottom: 5px;"></div> <div style="text-align: center; font-size: 0.8em;">(Give name in full)</div>		
<div style="border-top: 1px dashed black; height: 1.2em; margin-bottom: 5px;"></div> <div style="text-align: center; font-size: 0.8em;">(Street and number)</div>		
<div style="border-top: 1px dashed black; height: 1.2em; margin-bottom: 5px;"></div> <div style="font-size: 0.8em;">(Post office)</div>	<div style="border-top: 1px dashed black; height: 1.2em; margin-bottom: 5px;"></div> <div style="font-size: 0.8em;">(County)</div>	<div style="border-top: 1px dashed black; height: 1.2em; margin-bottom: 5px;"></div> <div style="font-size: 0.8em;">(State)</div>
Have you been advised by Bureau letter of your exemption? _____ If so, state <div style="text-align: right; font-size: 0.8em;">(Yes or no)</div> date of letter and subsection of section 101 under which you are exempt _____ <div style="border-top: 1px dashed black; height: 1.2em; margin-top: 5px;"></div>		
State nature of your activities _____ <div style="border-top: 1px dashed black; height: 1.2em; margin-top: 5px;"></div>		

The top line of the form, entitled "For Calendar Year _____," should be filled in with the year for which the return is made *only* if your organization's fiscal year is the *same* as the calendar year. Similarly, the second line should be entered with the inclusive dates of your organization's fiscal year *only* when that year *differs* from the calendar year. Obviously, therefore, only one line or the other should be used by a reporting organization.

On the name line should be entered (in typing or hand printing) the full official name of your organization. Check the exact name with that appearing in your cooperative's State charter, its articles of incorporation, or other organizational papers.

Next should be set down the full address. This should be where the main office and official records of your organization are located.

For most farmers' cooperatives which file this return, the answer to the first question will be "Yes." However, for organizations which have applied (on Treasury Department form 1028) for a letter of exemption but have not yet received such a letter, the correct answer is "No." In the latter case, the following notation should be made on the next line: "Proof of exemption under subsection 12 [or 13, as the case may be] was filed on form 1028 on [state date] but exemption letter has not yet been received."

If your organization has received a letter of exemption from the Commissioner of Internal Revenue, the date of the letter and the subsection of section 101 under which exemption was obtained should be inserted in the space shown.⁴ Exempt farmers' marketing and/or purchasing cooperatives should enter the words, "Subsection 12." Exempt farmers' cooperatives (organized and operated in conjunction with exempt farmers' marketing or purchasing associations) engaged in the financing of crop operations, should enter, "Subsection 13."

⁴If the letter of exemption is dated some years back, it may refer to an earlier version of the Internal Revenue Code, whose section numbers may differ from those mentioned herein.

If the letter of exemption has been mislaid or lost, it is desirable to obtain a photostatic copy thereof. This may be done by writing a letter to the Commissioner of Internal Revenue; Attention: Records Division, Income Tax Unit, Washington 25, D. C.⁵ The request must be signed by two officers of your organization and must bear its official seal, if it has a seal.

On the next line should be stated the nature of your organization's main activities. One, or a combination, of the following will be the usual answer for farmers' cooperatives:

- (a) Cooperative marketing of farmers' products.
- (b) Cooperative purchasing of farmers' supplies and equipment.
- (c) Cooperative bargaining relating to the marketing of farmers' products.
- (d) Cooperative servicing or processing connected with marketing of farmers' products.
- (e) Cooperative servicing or processing connected with the purchase of farmers' supplies and equipment.
- (f) Cooperative servicing or processing connected with the production of farmers' crops.
- (g) Cooperative financing of crop production.

PREPARATION OF LOWER PORTION OF PAGE 1, REVISED FORM 990

Page 1, Item 1. - "What is the legal form of your organization (corporation, trust, unincorporated association, etc.)?"

One of the following is the correct answer for a farmers' cooperative:

- (a) A corporation.
- (b) An unincorporated association.

Page 1, Item 2. - "In what year was your organization formed _____
In what State or country? _____"

The correct date and locality should be entered from the proper organizational paper, usually the charter or the articles of incorporation.

Page 1, Item 3. - "If this is your first return under your present name, indicate whether (a) completely new organization ☐ or (b) successor to previously existing organization(s) ☐. If successor to previously existing organization(s), give name(s) and address(es) of the predecessor organization(s)."

⁵The charge for photostating is 25 cents per page. Letters of exemption are usually of one page, therefore, 25 cents may be enclosed, preferably in noncurrency form, but not in postage stamps.

Enter an X-mark in one of the two blocks, as applicable. The term "predecessor organization" or "previously existing organization" is intended to apply not only to any former name of your organization but also to the entities included in any consolidation or merger and to any organization no longer in business whose property or whose functions, in part or in whole, were taken over or replaced by your organization.

Page 1, Item 4. - "Enter the approximate number of members (if a cooperative) or stockholders at the close of the year. Members _____ Stockholders: Preferred _____; Common _____."

Farmers' cooperatives formed on a capital stock basis are required to enter here the number of preferred and common stockholders. *All* reporting farmers' cooperatives must enter the approximate number of members as of the *close* of the year for which the return is made.

What constitutes a member depends entirely upon each organization's legal set-up as evidenced usually in its bylaws or other legal papers. It is important, of course, not to count as a member any person (or entity) who is merely a patron and who has not yet fulfilled the requirements for membership. If your organization's papers are not clear on the point, it may be assumed that any producer-patron who has a right to vote on the conduct of the association's affairs is a member.

Page 1, Item 5. - "If you have capital stock issued and outstanding, state with respect to each class of stock (a) the number of shares outstanding, (b) the number of shares held by individuals, (c) the number of shares held by organizations, and (d) whether any dividends may be paid."

If your organization is not formed on a capital stock basis, this item should be entered: "No capital stock."

If capital stock is issued and outstanding, the following is an illustrative entry. (If space is too small, attach a separate sheet.)

Items	Preferred stock	Common stock
Number of shares outstanding:		
Held by individuals.....	26	342
Held by organizations.....	2	18
Total shares outstanding.....	28	360

Dividend requirements:

Preferred stock.. 4% noncumulative

Common stock..... Maximum 6% when declared

In entering this item care should be taken to state the dividend requirements and rate accurately. Attention is directed to the fact that tax-exempt farmers' cooperatives having capital stock must not fix the rate of dividends thereon to exceed the legal rate of interest in the state of incorporation, or 8 percent per annum, whichever rate is greater.

In item 5 the term "whether any dividends may be paid" calls for information regarding your organization's legal power and obligation to declare dividends on capital stock according to its organizational papers and not to the probability of dividends being declared. Some associations are so organized as to preclude the payment of such dividends.

Page 1, Item 6. - "Are you affiliated with any other organization whether or not tax exempt?_____If so, give name of organization and nature of affiliation."

The word "affiliated" as here used refers to any entities connected with your organization (at any time during the reporting period) through your ownership of them, in part or whole; through their ownership of your organization, in part or whole; through your membership in them, or their membership in your organization; or through a close operating arrangement, whether or not actual ownership or membership is involved.

For those answering "yes" to this question, there follows a typical variety of possible entries for the second half of this item:

- (a) AA Farmers' Marketing Cooperative, St. Paul, Minnesota. They own 56% of our capital stock. We are members of this cooperative and ship some of our products through them for marketing.
- (b) BB Farmers' Purchasing Cooperative, Duluth, Minnesota. We own about 10% of their membership capital. Our packing supplies are purchased through them.
- (c) CC Farmers' Marketing Cooperative, Minneapolis, Minnesota. We are members of this organization and ship part of our products through them. No ownership connection.
- (d) DD Farmers' Marketing and Purchasing Cooperative, Somepoint, Minnesota. Pursuant to contract they handle sale of practically all of our products in terminal market. Some supplies are also purchased through them. No ownership or membership connection.
- (e) EE Supply Association, Anywhere, Minnesota. Most of our farm supplies are purchased through them. No direct ownership or membership connection, but they and we both are members of the central organization, the FF Central Cooperative.

Page 1, Item 7. - "State the names and addresses of the officers or other persons having care of the books of account, minutes, correspondence, and other documents and records of the organization."

This is self-explanatory.

Page 1, Item 8. - "Have any changes not previously reported to the Bureau been made in your articles of incorporation or bylaws or other instruments of similar import?_____ If so, attach a copy of the amendments."

The answers to both items 8 and 9 will enable the Bureau of Internal Revenue to study the legal and operating changes and to determine their effect on your organization's tax-exempt status.

Page 1, Item 9. - "Have you had any sources of income or engaged in any activities which have not previously been reported to the Bureau?_____If so, attach detailed statement."

If, during the reporting period, your organization had any new or revised forms of operating activity such changes should be reported under item 9, unless activities of the same or similar nature had been previously reported to the Bureau.

For instance, any significant change in the form of a marketing agreement with patrons or in the manner of paying or crediting patronage distributions (refunds or dividends) should be reported. Other reportable changes would be transactions such as the recent leasing of idle property or the sale of an outlying plant; and operating changes such as the opening of a department for purchase of supplies or for processing of farm products, in addition to your regular marketing operations, etc.

Minor changes in the method of pooling or distributing sales proceeds need not be reported but any fundamental change therein, such as the adoption of an entirely new and different method, should be explained to the Bureau, at least, in brief general terms. Any new or revised arrangement for the contribution of capital by patrons should be commented upon. This would include any new or revised agreement with the members or patrons, such as one permitting your association to retain patronage distributions (dividends, refunds, etc.) as a loan from the members or patrons, or as a temporary or permanent contribution to your association's capital, etc.

When marketing organizations merely shift to another agricultural product, or take on the handling of a new farm product, with no fundamental difference from the previous form of operation, it is not necessary to report such changes.

Similarly, no report need be made by purchasing cooperatives when they merely change their variety of supplies or services, unless such change fundamentally affects the style or manner of their operations. Thus, if a purchasing cooperative which keeps records of the business done with each patron were to add a retail gasoline sales department which it operated *without* a tabulation of each patron's purchases, that fact should be reported as it constitutes a fundamental change. The Bureau should have an opportunity of determining the effect of such a change on the organization's tax-exempt status.

Page 1, Item 10. - "Do you derive any rents or royalties from property which you have purchased from the lessee?_____Is any property of the organization leased or rented to, or does the organization lease or rent any property from, any person or groups of persons directly associated with the organization filing this return?_____.If either answer is 'yes,' give a detailed statement."

Although these two questions are *not* directed primarily to farmers' cooperatives, they must be answered by them.

The first question refers to the situation where property (usually real estate or patent rights) has been purchased by your organization and then leased to the seller.

The second question might be answered by considering the term "directly associated" as relating to the *same* entities already reported as affiliated under item 6, page 1, of revised form 990 and, additionally, to any officer, director, employee, or member of your organization, or of the affiliated organizations.

Page 1, Item 11. - "Check whether this return was prepared on the cash ☐ or accrual ☐ basis."

This refers to the type of accounting method used by your organization. Most farmers' cooperatives today use the accrual basis of accounting.

Page 1, Item 12. - "If you were held exempt under section 101(4), state the total amount of mortgage loans made during the year to (a) members, \$_____; (b) nonmembers, \$_____."

Page 1, Item 13. - "If you were held exempt under section 101(6), state whether any of your activities consisted of carrying on propaganda or otherwise attempting to influence legislation_____. If so, attach detailed statement."

Items 12 and 13 do not apply to, and therefore should not be entered by, farmers' cooperatives exempt under sections 101(12) and 101(13) of the Internal Revenue Code (or earlier corresponding sections).

Page 1, Item 14. - "Farmers' cooperative marketing and purchasing organizations shall also state --"

Page 1, Item 14(a). - "Number of shares of voting stock owned by (1) producers_____; (2) nonproducers_____."

Item 14(a) is designed to check on the observance of the tax-exemption provision which states that a farmers' cooperative having capital stock will not be denied exemption when substantially all of its voting capital stock is owned by producer-patrons.

Farmers' cooperatives, therefore, should be sure, in making entry under item 14(a), that *only* voting capital stock is reported. Although not asked for on form 990, it would be well to report in a footnote to this item any case where actual voting is on a basis other than the *number* of shares of stock.

Likewise, if the number of shares of voting stock held by nonproducers has increased since the prior annual return, an explanation of the circumstances of such increase should be made in a separate attached letter to the Bureau. Greater liberality is shown by the Bureau in cases where proof is given that the reporting association was powerless to prevent the stock acquisitions made by nonproducers.

If an association has the power to bar the holders of voting capital stock from voting when they are no longer producers, that fact should be reported.

Cooperatives exempt under either section 101(12) or 101(13) of the Code are required to answer item 14(a).

Page 1, Item 14(b). - "Were nonmembers charged the same as members for marketing and merchandise?"

The statutory tax-exemption provisions have been interpreted by many authorities to imply that exempt farmers' cooperatives must extend *equal treatment* to both member and nonmember patrons, at least in financial transactions. Compliance with this requirement is ascertained through item 14(b).

The Bureau's question is to be interpreted from the viewpoint of the *day-by-day* operations of your organization. Thus, if at all times throughout the reporting year it was the policy and practice of your organization to pay the *same* per-unit amount for a specified grade of farm product handled for either members or nonmembers; or to obtain the *same* amount for a specified quantity of any supply item purchased for either members or nonmembers, or for a particular type of servicing or processing rendered for either members or nonmembers; and, if it was the policy and practice to divide any net proceeds remaining at the year-end on the *same* patronage basis for both members and nonmembers, then your organization is justified in answering "yes" to question 14(b). In addition, it should be borne in mind that the law requires that nonmembers shall suffer no discrimination in the making of patronage distributions, in cash or otherwise.

Cooperatives exempt under either section 101(12) or 101(13) of the Code are required to answer question 14(b). However, as applied to organizations engaged in crop financing, under section 101(13), the question is intended to refer to the charging of interest and service fees. (Such items should be mentioned in the answer.)

Page 1, Item 14(c). - "State -	<u>Members</u>	<u>Nonmembers</u>
Sales to.....	\$ _____	\$ _____
Purchases for.....	_____	_____
Patronage dividends to....	_____	_____ "

Farmers' cooperatives are eligible for tax exemption when, among other things, the value of business with nonmembers does *not* exceed that done with members during each fiscal year, figured *separately* for marketing and purchasing operations.

The first line of this item entitled "Sales to" contains a typographical error. It should be changed to read "Sales for." On that line should be entered the value of farm products marketed for patrons and of any related service fees, separated as between member and nonmember business, for the reporting year. Do *not* include in either member or nonmember business the value of any products *marketed* for (or purchased from) the United States, or its agencies. The latter data should be shown *only* in item 14(f) below.

Note that the aggregate of entries made on the first line of item 14(c) should agree with the aggregate reported under item 14(d).

On the second line, entitled "Purchases for," those cooperatives having a purchasing business should enter, for the reporting year, the value of purchases (farm supplies and equipment) made for patrons and of any related service fees, separating member and nonmember business. Do *not* include in either member or nonmember business the value of any purchases made *for* the United States, etc. The latter data should be shown only in item 14(f) below.

Note that the aggregate of entries made on this second line should agree with the aggregate shown under item 14(e).

On the third line of item 14(c), entitled "Patronage dividends to," should be entered all forms of patronage distributions or allocations (patronage dividends or refunds, etc.) aggregated for *all* operations (marketing, purchasing, processing, servicing, etc.) whether paid in cash, or in noncash forms such as by issuance of certificates of debt, of capital stock, or of other equity or capital evidences; in capital equities merely credited by book entry; in credits to accounts receivable, etc.

Note that the amount entered here for "patronage dividends" must agree with the combined total of items 30 and 31, page 2, revised form 990. Since line 32, on page 2, covers the entry of any additions to capital reserves, it follows that such reserves (even though allocated to individual patrons) should be *excluded* from the "patronage dividends" reported under item 14(c) of page 1. (See discussion of reserves on pages 29 and 30.

Crop financing cooperatives, exempt under section 101(13) of the Code, are not required to answer item 14(c).

There has been some confusion as to the distinction between marketing and purchasing operations. A proper differentiation is important since in the statutory tax-exemption provisions operating receipts (or accruals) classed as purchasing activities have a 15 percent tolerance for dealings with nonproducers who are not members of the association. There is no such tolerance in the exemption provisions for business classified as marketing.

In reporting on revised form 990, the following definitions should be observed. Where a cooperative sells agricultural products furnished by its members or other patrons, or bargains or otherwise arranges for the sale of such products, the operating receipts (or accruals) on those activities must be classed as *marketing* operations. This is so whether the association physically handles the product, whether it actually receives and disburses the sales proceeds, and whether its reimbursement for expenses, etc. comes directly out of sales proceeds or through the medium of a commission, fee, or service charge.

Likewise, where an association performs for its members or other patrons a service connected with marketing, for example, cotton ginning, fruit packing, boxing and shipping, product storing, trucking of product inward, etc., the operating receipts (or accruals) on such activities are to be considered generally as *marketing* operations.

An association which engages in the purchasing of farm supplies and equipment for its members or other patrons, of course, must classify those activities as purchasing operations. This is true, also, of organizations which render a service connected with farm supplies and equipment; for example, corn grinding, seed cleaning, paint spraying, trucking, farm machinery repairing, rental of refrigerated lockers, etc. Generally, a service connected with crop production, such as spraying and dusting, picking, field boxing, etc., is classed, also, as a purchasing function.

Page 1, Item 14(d)⁶. - "Value of agricultural products marketed (or handled) for members (1) actually produced by such members, \$____; (2) purchased or otherwise acquired by such members, \$____; for nonmembers (1) actually produced by such nonmembers, \$____: (2) purchased or otherwise acquired by such nonmembers \$____."

If a tax-exempt farmers' marketing cooperative undertakes to handle agricultural products from *nonproducers or dealers*, or if it accepts products for the account of patrons (whether producers or nonproducers) who it knows did not *themselves* produce the particular product delivered, the cooperative runs a great risk of losing its tax-exempt status.

⁶ If there is a doubt about the distinction between a producer and a nonproducer, reference should be made to definitions discussed in paragraphs 189 through 202 of Bulletin 53 (refer to footnote (3) on page 3 herein).

Many cooperatives receive agricultural products for marketing from *another* farmers' cooperative, which products were produced by the latter's patrons. If your organization engaged in marketing during the reporting year for another such member-cooperative (whether or not the other organization is tax-exempt, but provided that, if not exempt, it is producer-owned and operated), such business should be shown as products marketed under the item 14(d) caption entitled "for members (1) actually produced by such members;" or, if the other cooperative is *not* a member of your organization, the business should be reported under the caption "for nonmembers (1) actually produced by such nonmembers." The same treatment should be given to products received from a corporation or partnership engaged in crop production.

Some cooperatives render certain services connected with marketing for a fee or commission, for example, packing and boxing, or cotton ginning, for a fee. Farmers' cooperatives operating in that manner should include such fees in item 14(d) and should add a footnote thereto making reference to a separate schedule. In that schedule should be reported, under the four subclassifications shown in item 14(d), the amount of the included fees or commissions. The total of such schedule should agree with an entry to be made under item 7, page 2, of revised form 990, using there the suggested subcaption "Fees from patrons for servicing, processing, etc., related to marketing."

Do *not* include in any classification under item 14(d) the value of any products marketed for (or purchased from) the United States or its agencies. That should be shown only in item 14(f) below.

It should be noted that the grand total of all entries under item 14(d) should agree with the total of the first line of item 14(c) and also with one or more entries to be made under item 7, page 2, of revised form 990, using there the suggested subcaption, "Gross sales proceeds from farm products marketed for patrons," and possibly others.

Crop financing cooperatives exempt under section 101(13) of the code are not required to answer item 14(d).

Page 1, Item 14(e)⁷. - "Value of supplies and equipment purchased for or sold to (1) members, \$____; (2) nonmembers who were producers, \$____; (3) nonmembers who were not producers, \$____."

Only farmers' cooperatives which handle supplies and equipment for their patrons or render related services, are required to make entries here. To retain its tax-exempt status, a farmers' cooperative must not purchase for nonmembers supplies whose total value during its fiscal year exceeds the total value of supplies purchased for and delivered to members. Furthermore, the purchases made for nonmembers by a tax-exempt cooperative

⁷If there is a doubt about the distinction between a producer and a nonproducer, reference should be made to the definitions discussed in paragraphs 189 through 202 of Bulletin 53 (refer to footnote (3) on page 3 herein).

are not to include purchases for nonproducers of a value more than 15 percent of the total value of all supplies delivered to patrons in the reporting year.

Supplies purchased for another cooperative organization may be classed as business done with a *producer*, whether the other organization is tax-exempt or not, but provided that, if not exempt, the other organization is producer-owned and operated.

Some farmers' cooperatives render services connected with supplies, for example, corn grinding or seed cleaning, for a fee. Organizations having service fees of that or similar type should include such amounts in item 14(e) and should add a footnote thereto making reference to a separate schedule. That schedule should report the included service fees under the three subclassifications shown in item 14(e). The total on such schedule should agree with an entry to be made under item 7, page 2, of revised form 990, using there the suggested subcaption, "Fees from patrons for servicing, processing, etc., related to supplies."

Where a significant amount of byproducts (from processing or manufacturing) are disposed of to nonmember nonproducers by a purchasing cooperative, the question of the proper place for reporting of such business should be taken up *directly* with the Bureau of Internal Revenue, Attention: Taxpayers' Rulings Section, Washington 25, D. C.

Some purchasing cooperatives at times order supplies on a sharing basis with some other local firm so as to obtain the mutual benefit of reduced prices and lower freight rates for a full carload lot. According to an informal Bureau ruling, the amount received from the other firm may be credited *directly* to the cost of purchases, instead of to "sales."

Do *not* include in any classification under item 14(e) the value of any purchases made for the United States or its agencies. That should be shown *only* under item 14(f) below.

The grand total of all entries under item 14(e) should agree with the total of the second line of item 14(c). These totals should agree, also, with one or more entries to be made under item 7, page 2, of revised form 990, using there the suggested subcaption, "Amounts received from patrons for supplies purchased for them," and possibly others.

Crop financing cooperatives exempt under section 101(13) of the Code are not required to answer item 14(e).

Page 1, Item 14(f). - "Amount of business done for United States Government or agencies thereof, \$_____."

Enter here the total value of business done for the United States Government or its agencies. This should include the value of products marketed, of processing done, of services rendered, and of agricultural products or other supplies purchased. It should *not* include the value of agricultural products *sold to* the United States Government, or any of its agencies,

when such values have *already* been reported under items 14(c) and 14(d) as marketing for members or nonmembers. However, if agricultural products purchased for the United States Government or its agencies were obtained from nonproducers or dealers, the value of such products should be included in the entry for item 14(f), but should *not* be reported under items 14(c), 14(d), or 14(e).

It should be borne in mind that no part of the amount entered in item 14(f) should appear in items 14(c), 14(d), or 14(e). Item 14(f), however, should agree with the total United States Government business reported under item 7, page 2, of revised form 990. (See suggested arrangement for item 7, as shown on page 22, hereof.)

Town, city, county, and State governmental units are *not* to be considered as agencies of the United States Government.

Crop financing cooperatives exempt under section 101(13) of the Code are not required to answer item 14(f).

PREPARATION OF OPERATING STATEMENT (On page 2 of Revised Form 990)

Necessary *minor* changes in the captions on page 2, of revised form 990, are permitted, but the general form thereof may not be changed, *nor may the form be replaced by submission of a separate copy of your organization's regular operating statement.*

It is important to understand clearly the nature and use of the statement on page 2. It is to be used in either of two ways, namely, (1) for the accrual basis of accounting, or (2) for the cash basis of accounting.

Accrual Basis

As used by farmers' cooperatives *reporting on the accrual basis*, page 2 is an annual statement of cooperative operations drawn up in special form to show the *entire* disposition of proceeds. It sets forth in the upper section, entitled "Income, Dues, Contributions, etc.," not only the receipts and accruals of relatively minor incidental items, but also the receipts and accruals of non-income nature derived from the main cooperative-agency functions of marketing, purchasing, servicing, and processing done for patrons.

Likewise, in the lower section, entitled "Disposition of Income, Dues, Contributions, etc.," there are to be listed by farmers' cooperatives *reporting on the accrual basis*, not only the payments and accruals of operating and incidental expenses of the organization, but also its base purchase cost of supplies delivered to patrons, or of supplies used in processing done for patrons; the payments made or credited to patrons for their products received; and finally the entire disposition of any remaining proceeds (net savings) at the year-end, in the form of cash or noncash patronage distributions (patronage dividends or refunds, etc.); in

the form of an addition to capital reserves (allocated or allocable to individual patrons on a patronage basis); or in dividends on capital stock, etc.

On the accrual basis, page 2 is *not* to be used to record any receipts of a capital nature, nor any disbursements of such nature. (See discussion of capital items on pages 19, 23, and 25, hereof.) This observation is not intended to exclude the reporting on lines 30, 31, and 32 (on page 2) of patronage distributions (dividends, refunds, etc.) arising from the operations of the year under review (*only*); nor to exclude the reporting on line 9 of gain or loss on sale of capital assets.

Thus it will be seen that when page 2 is used on the accrual basis, the totals appearing on line 11 and on line 34 *must* agree.

Cash Basis

For the comparatively few farmers' cooperatives which *keep their books on the cash basis*, page 2 is to be used as a statement of receipts and disbursements *covering operations only*. In that form of statement the receipts and disbursements of nonoperating or capital nature should be excluded from page 2. Such items, however, should be shown in the reconciliation called for by instruction 7, page 4 of revised form 990. Such a reconciliation should be reported in the following approximate form by attaching a separate schedule:

Reconciliation of Cash for Revised Form 990

Total operating receipts, per item 11, page 2.....	\$10,000
Total operating disbursements, per item 34, page 2.....	<u>8,000</u>
Excess of operating receipts over operating disbursements.....	2,000
Total nonoperating (or capital) receipts.....	<u>1,000</u>
Sub-total.....	3,000
Total nonoperating (or capital) disbursements.....	<u>4,000</u>
Excess of total disbursements over total receipts.....	1,000
Cash balance at beginning of period, per item 1, page 3.....	<u>6,000</u>
Cash balance at end of period, per item 1, page 3.....	<u><u>\$5,000</u></u>

On the cash basis, all moneys received and all sums disbursed during the reporting year *that affect operations* should be entered under the appropriate captions on page 2 of revised form 990, irrespective of the year in which such items originated. Thus, collections of any operating receivables, and payments of any operating payables, should be included on page 2. Likewise, there should be included any receipts of patronage distributions or of dividends on capital stock from other organizations, or any payments of patronage distributions or of dividends on capital stock made by your own association, regardless of the year to which such distributions or dividends apply.

There should be excluded, however, from page 2 any receipts and disbursements of *nonoperating* nature. Such items usually would consist

of any loans received or made; purchase or sale of real estate, buildings, equipment, other fixed assets or investments (except as to the gain or loss on such a sale which should be shown on line 9 of page 2, and, as well, on schedule B, page 3); any purchase, issuance, or retirement of capital stock or other capital equities, etc. (except that the receipt or payment of patronage distributions by your association in *noncash forms* should be footnoted under item 8 or item 31, as explained herein on pages 23 and 29.

IMPORTANT NOTE

The following comments will be directed *almost entirely* to the accrual method of accounting. Proper allowance, therefore, must be made in interpreting the comments when applied by cooperatives operating on the cash basis.

Page 2, Item 1⁸. - "Dues, assessments, etc. from members, excluding service and other charges properly included under item 7."

Page 2, Item 2⁸. - "Dues, assessments, etc. from affiliated organizations."

Certain types of farmers' cooperatives operate with a membership entrance fee and/or annual membership dues. All such items, along with other fees, fines, penalties, and assessments (including per capita assessments) from members should be entered in item 1, page 2, provided they are not of the *capitalized* type. (The latter usually appear as a continuing account on the organization's balance sheet, while those of noncapital nature do not.)

There should *not* be shown under item 1 or 2 any fees (though inappropriately called "dues" by the association) received for specific services rendered; or fees measured by the volume of product marketed or purchased. Such fees belong under item 7, page 2, of revised form 990.

Do not include in item 1 any amounts received and accrued from affiliated organizations but show all such amounts under item 2 only.

Page 2, Item 3⁸. - "Contributions, gifts, grants, etc. received."

Farmers' cooperatives rarely would have anything to report under this caption.

Page 2, Item 4. - "Interest" - (received).

This covers interest received and accrued on investments, or on sizable loans (akin to investments) made to affiliated organizations. Operating interest, such as interest on receivables from patrons, etc., should be entered only under item 7, page 2. (See Item H page 22 hereof.)

Similarly, for crop financing organizations exempt under section 101(13) of the Internal Revenue Code, interest on outside investments should be reported under item 4, while interest on loans receivable should be shown under item 7, page 2, of revised form 990.

⁸Note that instruction 5, on page 4 of revised form 990, refers to items 1, 2, 3, and 10 of page 2, and calls for itemization of certain amounts.

Page 2, Item 5. - "Dividends" - (received).

Enter here all dividends received and accrued on capital stock owned in other organizations. "Patronage dividends" or refunds received should *not* be entered here, but rather in item 8.

Page 2, Item 6. - "Rents" - (received).

Entry should be made here of all rents received and accrued (gross) for occupancy of property owned or subleased by your organization. Upkeep expenses of such rented property should appear within items 16 through 19, page 2.

Page 2, Item 7. - "Gross receipts from business activities."

Under this item are to be listed the amounts received and accrued which arise from the *primary functions* of farmers' cooperatives, namely, from marketing, purchasing, and related operations. On page 22 is table A, showing a suggested variety of subcaptions for insertion when applicable under item 7. If the subcaptions actually reported are too numerous to fit into the available space on the form under item 7, then a separate schedule should be attached.

Other receipts and accruals closely related to the types shown on table A should be listed also under item 7, with appropriate subcaptions. Freight charges outward may be directly deducted from item (a) of table A, if desired.

Some marketing cooperatives (notably those dealing in wool) may sell the crop of one year over a period of years, maintaining a continuing sales-and-expense pool for *each crop*. The sales proceeds, the corresponding expenses, and the corresponding pool payments made or credited to patrons during the *entire* selling period for a particular crop should be accumulated and reported on the proper lines of page 2, revised form 990, for the fiscal year in which the crop pool is finally closed, *regardless* of when the concerned crop was grown. (See also discussion of patronage distributions on page 28, hereof.)

The total of business done for the United States Government or its agencies, as shown under item 7, page 2, of revised form 990, (or per column 2 of table A on page 22 hereof), should agree with the total entered as item 14(f) on page 1, revised form 990.

Patronage distributions (patronage dividends, refunds, etc.) made by a purchasing cooperative should *not* be deducted from item 7, but should be reported separately in item 30 or 31, as the case may be. Similarly, the amounts received from patrons for their purchases throughout the year, as reported in item 7, should *not* be divided into two parts, namely, (1) the amount of the patronage distribution and (2) the amount received from patrons for purchases, adjusted (reduced) by application of the patronage distribution.

TABLE A

TYPICAL ENTRIES FOR ITEM 7, PAGE 2, OF REVISED FORM 990
 "Gross Receipts from Business Activities"

Description (1)	Business for	
	U. S. A. (2)	All others (3)
(a) Gross sales proceeds from farm products marketed for patrons (often referred to as "sales") ¹	\$_____	\$_____
(b) Amounts received from patrons for supplies purchased for them (often referred to as "sales").....	\$_____	\$_____
(c) Fees from patrons for servicing, processing, etc. related to marketing.....	\$_____	\$_____
(d) Fees from patrons for servicing, processing, etc. related to supplies.....	\$_____	\$_____
(e) Service fees (or commissions) from patrons for marketing of their products.....	\$_____	\$_____
(f) Fees from patrons for bargaining services rendered ¹	\$_____	\$_____
(g) Interest (or other fees) from patrons for financing of patrons' crops.....	\$_____	\$_____
(h) Interest on receivables from patrons...	\$_____	\$_____
Grand total.....	\$_____	\$_____

¹Bargaining associations which handle the sales proceeds of patrons' products and also charge a fee for their services should report in both items (a) and (f) above.

Page 2, Item 8. - "Patronage dividends (or patronage refunds) received."

Enter on this line all patronage distributions (patronage dividends, refunds, etc.) received, or accrued as a receivable, from other cooperative organizations during the reporting year. All such distributions should be included whether received (or to be received) in cash, or in noncash forms such as in capital stock, notes, book credits, or other evidence of equity or indebtedness.

Under item 8 must be reported *all* patronage distributions (whether in cash or noncash form) received, or accrued as a receivable, from other organizations even though it is your association's practice to simply redistribute such items to its concerned patrons *without* any entry on your regular operating statement. (The redistribution to patrons, likewise, must be reported within item 30, 31, or 32, as the case may be, on page 2, revised form 990. See page 29 hereof.)

Ordinarily, such patronage distributions are reportable by the *receiving* cooperative on page 2 for the *same year* in which they *arose* on the records of the *issuing* cooperative, or in which the latter set them up as a payable. When that is not possible, they should be reported as an accrual in the year in which the receiving organization obtains its *first advice* of the amount concerned. Thus, for example, if a crop pool for 1944 is finally closed late in 1946, and patronage distributions thereon are announced as a payable by the issuing cooperative say in February 1947, the distributions should be reported by the receiving organization in its 1946 return on revised form 990, unless its books for 1946 have been closed. In the latter event, report should be made in the 1947 return. Entry should *not* be deferred until actual receipt of cash.

Cooperatives which keep their books on the cash basis and which receive a patronage distribution in noncash form from another organization, should make a parenthetical notation thereof (showing the amount, etc.) on the line for item 8.

Repayments from other organizations of loans made by your cooperative; payments received on notes or other receivables; and payments to your organization by other entities to retire their capital stock or other forms of capital equities, should *not* be entered in item 8. In fact, such items are not reportable as receipts anywhere on page 2 of revised form 990 by organizations using the accrual method of accounting.

Page 2, Item 9. - "Gain (or loss) from sales of assets," etc.

If your association sold or junked any of its assets (excluding inventory items) during the reporting year, the gain or loss on such disposal should be figured by first filling in schedule B on page 3 of form 990. The total of column 8 of that schedule then should be entered (as a plus or minus figure) on the line for item 9, page 2. The assets of a farmers' cooperative most likely to appear on schedule B are physical property (real estate, capital equipment, etc.) and investments, patent rights, etc.

The foregoing paragraph applies to all reporting organizations whether they are on the cash basis or the accrual basis of accounting.

Page 2, Item 10. - "Other income."

All other types of receipts and accruals not previously entered should be combined and entered as item 10. Care should be taken to exclude from this entry (for reporting under item 7, page 2) all amounts which arise from cooperative functions performed for patrons.

As stated on form 990, when item 10, page 2, amounts to more than 10 percent of item 11, an itemized schedule of item 10 should be attached.

Page 2, Item 11. - "Total of items 1 to 10, inclusive."

This is simply a line for the totalling of receipts and accruals. It should agree with the total shown as item 34, page 2, if your organization is reporting on the accrual basis. Instruction 7, on page 4 of revised for 990, mentions a reconciliation schedule. Such a schedule is desirable for an organization reporting on the cash basis of accounting (see page 18 hereof). On the accrual basis, however, if page 2 is drawn up properly no such reconciliation will be necessary as items 11 and 34 will agree.¹⁰

Page 2, Caption "A." - "Expenses attributable to income items 6 and 7."

While this caption uses the word "expenses" it is to be understood that the amounts appearing under item 12 are not technically expenses in the case of cooperative operations. (See discussion below.)

Page 2, Item 12. - "Purchases for or advances to patrons."

It is seen that, for farmers' cooperatives, this line is to be used for several different purposes. One or more of the following elements usually will appear under item 12:

- (a) Amounts paid or credited during the year to patrons for their farm products sold (often referred to as "purchases").
- (b) Association's base purchase cost of farm supplies and equipment purchased for and delivered to patrons during the year.

Note: This is net, after application of inventories values.

- (c) Association's base purchase cost of supplies used during the year in processing or manufacturing done for patrons. (Other items of processing or manufacturing cost should *not* be reported here, but rather among items 13 through 19, page 2 of revised form 990.)

Note: This is net, after application of inventories values.

Other advances, payments, and accruals closely related to the foregoing types should be included also under item 12. Freight charges inward may

¹⁰This differs from the old form 990 which was not designed so as to produce an agreement in these totals.

be directly added to items (b) and (c) above, if desired. See discussion on page 21, hereof, concerning the handling of continuing crop pools.

Patronage distributions (patronage dividends, refunds, etc.) made by a reporting marketing cooperative should *not* be added to item 12, but should be reported separately under item 30, 31, or 32, page 2, revised form 990. (See further discussion on page 28.)

Some farmers' cooperatives obtain funds for capital purposes (usually on account of capital stock, capital shares, or other capital equities) from patrons through authorized deductions of a fixed amount, or an amount-per-unit-shipped, from the sales proceeds of patrons' products. The capital amounts so obtained by an association should *not* be deducted from the *gross amount* of payments made or credited to patrons in reporting on line 12. Or, to put it more clearly, the capital amounts should be added to the net payments made to patrons so that the *gross amount* will be shown on line 12.

The same handling applies to any amount deducted from a patron's marketing proceeds and forwarded, upon his authority and for his account, to outside organizations or persons.

Crop financing cooperatives, exempt under section 101(13) of the code, normally will have no entry for item 12.

Page 2,

- Item 13. - "Compensation of officers, directors, trustees, etc."
- Item 14. - "Wages, salaries, and commissions." - [other than next above]
- Item 15. - "Interest" - [paid]
- Item 16. - "Taxes (such as property, income, social security, unemployment, etc.)"
- Item 17. - "Rent" - [paid]
- Item 18. - "Depreciation."
- Item 19. - "Miscellaneous expenses (state nature)."

In this group of operating expenses on page 2, under the caption "A", it is intended to record the expenses applicable to the main cooperative-agency functions of a farmers' organization. Those functions are typified in the list shown on page 22 of this report. Included in group "A", also, should be any expenses found applicable to owned or leased properties which are rented to others. Such expenses usually would consist of taxes, depreciation, repairs, etc.

If an individual happens to be both a director and an employee (such as a manager) it is desirable that his compensation as a director be shown under item 13, while his compensation as an employee should be listed under item 14.

Do not include in item 15 - "Interest" - any dividends paid by your organization on capital stock. Such payments are to be shown only in item 29, page 2, of revised form 990.

Item 19 should include bad debts expense, if any.

Do not include in group "A" any expenses which properly belong in group "B", items 20 through 26, page 2, revised form 990. (See explanation below of group "B" items.)

Page 2, Caption "B". - "Other expenses":

- Item 20. - "Dues, assessments, etc. to affiliated organizations."
- Item 21. - "Compensation of officers, directors, trustees, etc.
(Not included under item 13)."
- Item 22. - "Wages, salaries, and commissions (not included under item 14.)"
- Item 23. - "Interest (not included under item 15)."
- Item 24. - "Taxes (not included under item 16)."
- Item 25. - "Rent (not included under item 17)."
- Item 26. - "Miscellaneous expenses not elsewhere classified."

Except for item 20, very few, if any, farmers' cooperatives will have entries to make under group "B" expenses, since the latter consist of items *not* applicable either to the organization's main cooperative functions (reported under item 7) or to rents received (item 6). Practically the only instance in which a farmers' cooperative would find it necessary to segregate any expenses into group "B" (excepting item 20) arises where its investments, of interest- or dividend-earning nature, were so numerous and extensive as to require for their handling either a measurable amount of the management's time, or actually a separate staff. Such a situation would be extremely rare, if it exists at all.

The Bureau's instruction 6, on page 4 of revised form 990, should be carefully read for further information on the methods acceptable for allocation of expenses to group "B" in the rare cases when such allocation may be found necessary for farmers' cooperatives.

It is the intention of the Bureau of Internal Revenue that the dues, etc., described in item 20 shall be entered *only* under item 20 and not among the group "A" expenses. Payments to affiliated organizations, in the nature of capital contributions or capital equity purchases by your association, should *not* be entered under item 20, nor, in fact, anywhere on page 2 of revised form 990 for those reporting either on the cash or the accrual basis.

Do not repeat in group "B" any amounts which have already been reported under group "A" expenses.

Page 2, Caption "C". - "Contributions";

- Item 27. - "Contributions, gifts, grants, etc. paid."

Do not include this type of expense under any other item on page 2. Note that itemization of payee's name and amount is required.

Page 2, Caption "D". - "Other Dispositions."

Item 28. - "Benefit payments to or for members or their dependents."

This item is designed for use primarily by organizations other than farmers' cooperatives. Nevertheless, a farmers' cooperative at times may have a payment that corresponds in some measure with the described item.

Page 2, Item 29. - "Dividends (other than patronage dividends) and other distributions to members, shareholders, or depositors."

Usually the only type of distribution to be entered on this line by certain farmers' cooperatives would be dividends on capital stock. It should be understood that such dividends on capital stock are to be entered here *only* when declared out of the net proceeds *originating* in the reporting year, whether or not they are paid within that year.

Sometimes a dividend on capital stock is declared in one year out of the proceeds of the prior year. When such a declaration occurs before the closing of the association's books for the prior year, or *before* the filing of revised form 990 for the prior year, the latter, when filed, should show the dividend under item 29. If, however, the declaration is not made until *after* the filing of revised form 990 for the prior year, then an amendment of such return should be made by writing a letter outlining the declaration amount, etc., to the Bureau of Internal Revenue; Attention: Taxpayer's Ruling Section, Washington 25, D. C.

Page 2, Item 30. - "Cash patronage dividends (or patronage refunds)."

Page 2, Item 31. - "Patronage dividends (or patronage refunds) in stock, notes, credits, or other evidence of equity or indebtedness."

These two items cover the entries for patronage distributions (dividends, refunds, etc.) *made or accrued* during the reporting year by your organization. Item 30 is for distributions, arising from operations of the reporting year, actually paid in cash *before* filing of the revised form 990 for that year. Item 31 covers similar distributions made or to be made in noncash forms, as described in the caption above, or those to be paid in cash but not yet so paid at the filing date of revised form 990.

Organizations which are engaged in *both* marketing and purchasing activities are not required to distinguish "patronage dividends" of the marketing department from those of the purchasing department. It is recommended, however, that such separation be reported in a footnote to items 30 or 31.

It is again emphasized that the entry here of patronage distributions should be limited to those arising from operations *originating* in the reporting year or from crop pools *finally closed* in that year. Thus, if a patronage distribution arising from, say, 1945 operations (or from pools closed in 1945) was actually paid off in cash during 1946 *before* the filing date of the annual return, it should be reported under item 30 of form 990 for the year 1945, but it is not reportable at all on page 2 for the year 1946.

Some exempt associations at times declare the details of patronage distribution in *one year* covering the net proceeds remaining at the close of the *prior year*. Such declarations should be entered as item 30, 31, or 32, on the return for the *prior year* and should not appear in any place on page 2 of the return for the *year in which the actual declaration was made*. (Delayed declaration of patronage distributions, as described, is not a good practice for nonexempt cooperatives and it may not be such a good practice for certain tax-exempt cooperatives. In the case of exempt associations *organized with a proper legal and cooperative structure*, all remaining net proceeds at the year-end belong, in any event, to the year's patrons. Declarations, therefore, for such associations usually are needed only to state the form (cash or noncash) of payment of the distributions, when such form is selective at the option of the directors.)

Some marketing associations in the past have erroneously reported as patronage distributions the basic payments (or credits) made to patrons for their products delivered to the association. For the purpose of reporting on revised form 990 the following definitions should govern. In the case of associations like creameries which operate by means of sales pools closed semi-annually, quarterly, monthly, or oftener, the payments (or credits) made to patrons from each sales pool are to be entered in the aggregate on line 12 and thus are not to be considered as patronage distributions. If, however, such an association makes a prorata additional payment (or credit) to the patrons of *more than one pool*, it is to be considered as a patronage distribution reportable as item 30, 31, or 32.

Other marketing cooperatives such as grain elevator associations operate by paying the approximate current market price upon delivery by patrons of their products. Payments of that kind are to be reported on line 12. The sum usually calculated semi-annually or annually by such organizations as a prorata additional payment (or credit) to each patron is to be considered as a patronage distribution for entry as item 30, 31, or 32, as the case may be.

It has been felt by some cooperative authorities that when patronage distributions of a marketing cooperative are paid in the form of capital stock, or of other capital equities, the amounts so involved should not be reported as a specific patronage distribution but should be added *directly* to the reported payments made to patrons for products received during the year. This follows the theory that the amounts were *constructively received* by the patrons and, in turn *constructively turned back* to the association as a contribution to capital. That theory, while tenable, should not be used in preparing the revised form 990. (See also similar discussion on page 25.)

Some wool marketing cooperatives, and perhaps other types, operate with sales pools that continue over several years for a particular crop (as discussed on page 21 hereof). Any patronage distributions made on such a crop pool should be reported under item 30, 31, or 32, as the case may be, for the fiscal year in which the pool was finally closed, *regardless* of when the concerned crop was grown.

Page 2, Item 5. - "Dividends" - (received).

Enter here all dividends received and accrued on capital stock owned in other organizations. "Patronage dividends" or refunds received should *not* be entered here, but rather in item 8.

Page 2, Item 6. - "Rents" - (received).

Entry should be made here of all rents received and accrued (gross) for occupancy of property owned or subleased by your organization. Upkeep expenses of such rented property should appear within items 16 through 19, page 2.

Page 2, Item 7. - "Gross receipts from business activities."

Under this item are to be listed the amounts received and accrued which arise from the *primary functions* of farmers' cooperatives, namely, from marketing, purchasing, and related operations. On page 22 is table A, showing a suggested variety of subcaptions for insertion when applicable under item 7. If the subcaptions actually reported are too numerous to fit into the available space on the form under item 7, then a separate schedule should be attached.

Other receipts and accruals closely related to the types shown on table A should be listed also under item 7, with appropriate subcaptions. Freight charges outward may be directly deducted from item (a) of table A, if desired.

Some marketing cooperatives (notably those dealing in wool) may sell the crop of one year over a period of years, maintaining a continuing sales-and-expense pool for *each crop*. The sales proceeds, the corresponding expenses, and the corresponding pool payments made or credited to patrons during the *entire* selling period for a particular crop should be accumulated and reported on the proper lines of page 2, revised form 990, for the fiscal year in which the crop pool is finally closed, *regardless* of when the concerned crop was grown. (See also discussion of patronage distributions on page 28, hereof.)

The total of business done for the United States Government or its agencies, as shown under item 7, page 2, of revised form 990, (or per column 2 of table A on page 22 hereof), should agree with the total entered as item 14(f) on page 1, revised form 990.

Patronage distributions (patronage dividends, refunds, etc.) made by a purchasing cooperative should *not* be deducted from item 7, but should be reported separately in item 30 or 31, as the case may be. Similarly, the amounts received from patrons for their purchases throughout the year, as reported in item 7, should *not* be divided into two parts, namely, (1) the amount of the patronage distribution and (2) the amount received from patrons for purchases, adjusted (reduced) by application of the patronage distribution.

TABLE A

TYPICAL ENTRIES FOR ITEM 7, PAGE 2, OF REVISED FORM 990
"Gross Receipts from Business Activities"

Description (1)	Business for	
	U. S. A. (2)	All others (3)
(a) Gross sales proceeds from farm products marketed for patrons (often referred to as "sales") ¹	\$_____	\$_____
(b) Amounts received from patrons for supplies purchased for them (often referred to as "sales").....	\$_____	\$_____
(c) Fees from patrons for servicing, processing, etc. related to marketing.....	\$_____	\$_____
(d) Fees from patrons for servicing, processing, etc. related to supplies.....	\$_____	\$_____
(e) Service fees (or commissions) from patrons for marketing of their products.....	\$_____	\$_____
(f) Fees from patrons for bargaining services rendered ¹	\$_____	\$_____
(g) Interest (or other fees) from patrons for financing of patrons' crops.....	\$_____	\$_____
(h) Interest on receivables from patrons...	\$_____	\$_____
Grand total.....	\$_____	\$_____

¹Bargaining associations which handle the sales proceeds of patrons' products and also charge a fee for their services should report in both items (a) and (f) above.

Page 2, Item 8. - "Patronage dividends (or patronage refunds) received."

Enter on this line all patronage distributions (patronage dividends, refunds, etc.) received, or accrued as a receivable, from other cooperative organizations during the reporting year. All such distributions should be included whether received (or to be received) in cash, or in noncash forms such as in capital stock, notes, book credits, or other evidence of equity or indebtedness.

Under item 8 must be reported *all* patronage distributions (whether in cash or noncash form) received, or accrued as a receivable, from other organizations even though it is your association's practice to simply redistribute such items to its concerned patrons *without* any entry on your regular operating statement. (The redistribution to patrons, likewise, must be reported within item 30, 31, or 32, as the case may be, on page 2, revised form 990. See page 29 hereof.)

Ordinarily, such patronage distributions are reportable by the *receiving* cooperative on page 2 for the *same year* in which they *arose* on the records of the *issuing* cooperative, or in which the latter set them up as a payable. When that is not possible, they should be reported as an accrual in the year in which the receiving organization obtains its *first advice* of the amount concerned. Thus, for example, if a crop pool for 1944 is finally closed late in 1946, and patronage distributions thereon are announced as a payable by the issuing cooperative say in February 1947, the distributions should be reported by the receiving organization in its 1946 return on revised form 990, unless its books for 1946 have been closed. In the latter event, report should be made in the 1947 return. Entry should *not* be deferred until actual receipt of cash.

Cooperatives which keep their books on the cash basis and which receive a patronage distribution in noncash form from another organization, should make a parenthetical notation thereof (showing the amount, etc.) on the line for item 8.

Repayments from other organizations of loans made by your cooperative; payments received on notes or other receivables; and payments to your organization by other entities to retire their capital stock or other forms of capital equities, should *not* be entered in item 8. In fact, such items are not reportable as receipts anywhere on page 2 of revised form 990 by organizations using the accrual method of accounting.

Page 2, Item 9. - "Gain (or loss) from sales of assets," etc.

If your association sold or junked any of its assets (excluding inventory items) during the reporting year, the gain or loss on such disposal should be figured by first filling in schedule B on page 3 of form 990. The total of column 8 of that schedule then should be entered (as a plus or minus figure) on the line for item 9, page 2. The assets of a farmers' cooperative most likely to appear on schedule B are physical property (real estate, capital equipment, etc.) and investments, patent rights, etc.

The foregoing paragraph applies to all reporting organizations whether they are on the cash basis or the accrual basis of accounting.

Page 2, Item 10. - "Other income."

All other types of receipts and accruals not previously entered should be combined and entered as item 10. Care should be taken to exclude from this entry (for reporting under item 7, page 2) all amounts which arise from cooperative functions performed for patrons.

As stated on form 990, when item 10, page 2, amounts to more than 10 percent of item 11, an itemized schedule of item 10 should be attached.

Page 2, Item 11. - "Total of items 1 to 10, inclusive."

This is simply a line for the totalling of receipts and accruals. It should agree with the total shown as item 34, page 2, if your organization is reporting on the accrual basis. Instruction 7, on page 4 of revised for 990, mentions a reconciliation schedule. Such a schedule is desirable for an organization reporting on the cash basis of accounting (see page 18 hereof). On the accrual basis, however, if page 2 is drawn up properly no such reconciliation will be necessary as items 11 and 34 will agree.¹⁰

Page 2, Caption "A." - "Expenses attributable to income items 6 and 7."

While this caption uses the word "expenses" it is to be understood that the amounts appearing under item 12 are not technically expenses in the case of cooperative operations. (See discussion below.)

Page 2, Item 12. - "Purchases for or advances to patrons."

It is seen that, for farmers' cooperatives, this line is to be used for several different purposes. One or more of the following elements usually will appear under item 12:

(a) Amounts paid or credited during the year to patrons for their farm products sold (often referred to as "purchases").

(b) Association's base purchase cost of farm supplies and equipment purchased for and delivered to patrons during the year.

Note: This is net, after application of inventories values.

(c) Association's base purchase cost of supplies used during the year in processing or manufacturing done for patrons. (Other items of processing or manufacturing cost should *not* be reported here, but rather among items 13 through 19, page 2 of revised form 990.)

Note: This is net, after application of inventories values.

Other advances, payments, and accruals closely related to the foregoing types should be included also under item 12. Freight charges inward may

¹⁰This differs from the old form 990 which was not designed so as to produce an agreement in these totals.

be directly added to items (b) and (c) above, if desired. See discussion on page 21, hereof, concerning the handling of continuing crop pools.

Patronage distributions (patronage dividends, refunds, etc.) made by a reporting marketing cooperative should *not* be added to item 12, but should be reported separately under item 30, 31, or 32, page 2, revised form 990. (See further discussion on page 28.)

Some farmers' cooperatives obtain funds for capital purposes (usually on account of capital stock, capital shares, or other capital equities) from patrons through authorized deductions of a fixed amount, or an amount-per-unit-shipped, from the sales proceeds of patrons' products. The capital amounts so obtained by an association should *not* be deducted from the *gross amount* of payments made or credited to patrons in reporting on line 12. Or, to put it more clearly, the capital amounts should be added to the net payments made to patrons so that the *gross amount* will be shown on line 12.

The same handling applies to any amount deducted from a patron's marketing proceeds and forwarded, upon his authority and for his account, to outside organizations or persons.

Crop financing cooperatives, exempt under section 101(13) of the code, normally will have no entry for item 12.

Page 2,

- Item 13. - "Compensation of officers, directors, trustees, etc."
- Item 14. - "Wages, salaries, and commissions." - [other than next above]
- Item 15. - "Interest" - [paid]
- Item 16. - "Taxes (such as property, income, social security, unemployment, etc.)"
- Item 17. - "Rent" - [paid]
- Item 18. - "Depreciation."
- Item 19. - "Miscellaneous expenses (state nature)."

In this group of operating expenses on page 2, under the caption "A", it is intended to record the expenses applicable to the main cooperative-agency functions of a farmers' organization. Those functions are typified in the list shown on page 22 of this report. Included in group "A", also, should be any expenses found applicable to owned or leased properties which are rented to others. Such expenses usually would consist of taxes, depreciation, repairs, etc.

If an individual happens to be both a director and an employee (such as a manager) it is desirable that his compensation as a director be shown under item 13, while his compensation as an employee should be listed under item 14.

Do not include in item 15 - "Interest" - any dividends paid by your organization on capital stock. Such payments are to be shown only in item 29, page 2, of revised form 990.

Item 19 should include bad debts expense, if any.

Do not include in group "A" any expenses which properly belong in group "B", items 20 through 26, page 2, revised form 990. (See explanation below of group "B" items.)

Page 2, Caption "B". - "Other expenses":

- Item 20. - "Dues, assessments, etc. to affiliated organizations."
- Item 21. - "Compensation of officers, directors, trustees, etc.
(Not included under item 13)."
- Item 22. - "Wages, salaries, and commissions (not included under item 14.)"
- Item 23. - "Interest (not included under item 15)."
- Item 24. - "Taxes (not included under item 16)."
- Item 25. - "Rent (not included under item 17)."
- Item 26. - "Miscellaneous expenses not elsewhere classified."

Except for item 20, very few, if any, farmers' cooperatives will have entries to make under group "B" expenses, since the latter consist of items *not* applicable either to the organization's main cooperative functions (reported under item 7) or to rents received (item 6). Practically the only instance in which a farmers' cooperative would find it necessary to segregate any expenses into group "B" (excepting item 20) arises where its investments, of interest- or dividend-earning nature, were so numerous and extensive as to require for their handling either a measurable amount of the management's time, or actually a separate staff. Such a situation would be extremely rare, if it exists at all.

The Bureau's instruction 6, on page 4 of revised form 990, should be carefully read for further information on the methods acceptable for allocation of expenses to group "B" in the rare cases when such allocation may be found necessary for farmers' cooperatives.

It is the intention of the Bureau of Internal Revenue that the dues, etc., described in item 20 shall be entered *only* under item 20 and not among the group "A" expenses. Payments to affiliated organizations, in the nature of capital contributions or capital equity purchases by your association, should *not* be entered under item 20, nor, in fact, anywhere on page 2 of revised form 990 for those reporting either on the cash or the accrual basis.

Do not repeat in group "B" any amounts which have already been reported under group "A" expenses.

Page 2, Caption "C". - "Contributions";

- Item 27. - "Contributions, gifts, grants, etc. paid."

Do not include this type of expense under any other item on page 2. Note that itemization of payee's name and amount is required.

Page 2, Caption "D". - "Other Dispositions."

Item 28. - "Benefit payments to or for members or their dependents."

This item is designed for use primarily by organizations other than farmers' cooperatives. Nevertheless, a farmers' cooperative at times may have a payment that corresponds in some measure with the described item.

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Some exempt associations at times declare the details of patronage distribution in *one year* covering the net proceeds remaining at the close of the *prior year*. Such declarations should be entered as item 30, 31, or 32, on the return for the *prior year* and should not appear in any place on page 2 of the return for the *year in which the actual declaration was made*. (Delayed declaration of patronage distributions, as described, is not a good practice for nonexempt cooperatives and it may not be such a good practice for certain tax-exempt cooperatives. In the case of exempt associations *organized with a proper legal and cooperative structure*, all remaining net proceeds at the year-end belong, in any event, to the year's patrons. Declarations, therefore, for such associations usually are needed only to state the form (cash or noncash) of payment of the distributions, when such form is selective at the option of the directors.)

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